Monday, 15 January 2024

KBC Sunrise Market Commentary

Markets

- Markets on Friday again took **somewhat of a biased reading,** both of the developments in the Middle East and the US eco data. The air strikes of the US and the UK against Houthi targets in Yemen **(temporarily) propelled Brent oil above $80 p/b.** However, the impact on other markets was a bit **diffuse.** Higher oil prices hardly affected yields and equity markets held in positive territory. **US PPIs,** a series that is often ignored especially when it is published after the CPI release, again showed markets' bullish bias towards bonds. **What can't go up, must come down.** On Thursday, a higher-than-expected CPI failed to trigger a further rebound in yields. A slightly softer than expected PPI (-0.1% M/M and 1.0% y/y, vs 0.1% and 1.3% expected) this time was seen as a good enough reason for the Fed to embark on an aggressive rate cut cycle this year. **In a outright steepening move,** the US 2-y yield declined 10.1 bps. The 30-y finished marginally higher (+0.25 bpn). Markets again discount a 75% chance of a first Fed rate cut in March and more than 150 bps of rate cuts by the end of the year. To be honest, we don't see how recent data (labour market data, CPI) would force the Fed for such an aggressive approach. **German yields,** which still had some catching up to do, also declined between 10.9 bps and (2-y) and 3.1 bps (10-y). For **equity investors,** softer monetary conditions still outweigh lingering (geopolitical) uncertainty. The EuroStoxx 50 gained 0.85%. US equities were little changed going into the long weekend. Still **no clear directional trend in the major FX cross rates.** The DXY USD index closed marginally higher at 102.4, perfectly in the middle of the ST 102/13 consolidation range. Similar story for EUR/USD (close 1.0951). The yen slightly outperformed on lower core yields (USD/JPY close at 144.88).
- This morning/today **trading in major markets is taking a slow start as US markets will be closed for Martin Luther King Day.** Asian equities are trading mixed with Japan still outperforming (Nikkei + 0.9%). The Japanese 2-y yield revisits the 0.0% barrier as investors see ever less urgency for the BoJ to make a policy U-turn anytime soon. **Today,** the eco calendar mainly contains data of secondary importance. **Later this week,** US retail sales (Wednesday) and Michigan consumer confidence (Friday) are interesting. **China** will release Q4 GDP data on Wednesday. Plenty of central bankers will also attend the World Economic Forum in Davos. Will they use the Forum to give an assessment on recent market positioning? Probably quite some clear speak from CB heavyweights is needed to amend current soft market reaction function. On FX markets EUR/USD is blocked in a tight sideways range between 1.0875 & 1.10. **EUR/GBP trading might become a bit more lively** compared to last week, with UK labour market data (Tuesday), inflation data (Wednesday) and retail sales (Friday) scheduled for release.

News & Views

- **Current vice president Lai Ching-te** won the p**residential elections in semiconductor-spewing Taiwan** on Saturday. The ballot in these heated geopolitical times was seen as the most pivotal one in decades. Lai of the ruling Democratic Progressive Party secured about 40% of the votes. He won from opposition parties willing to restart the dialogue with China after being suspended under DPP rule for eight years. Taiwan is now gearing up for a record third straight term under the party that seeks to minimize Chinese influence. That said, L**ai must look for a delicate balance in maintaining strong ties with major democracies including the US while avoiding (escalating) tensions with Beijing that could erupt into a conflict.**
- The **Chinese central bank kept a key policy rate steady at 2.5% this morning.** Expectations were for a slight cut to 2.4% after a series of disappointing data last week, including negative CPI and PPI growth and lower-than-expected credit growth. Instead, t**he PBOC opted for a liquidity injection that was larger than anticipated.** The weak yuan is seen as deterring the central bank from going all-in with rate cuts. Combined with uncertainty over the Fed policy rate (cut in March, May or even later?) the PBOC isn't willing to the jump the gun. USD/CNY eases marginally to 7.17 this morning. In October last year, the pair was trading around 7.3, the weakest CNY level since 2007**. A senior central bank official recently did say the central bank may cut the reserve requirement ratio, probably in Q1.** That would also unleash additional liquidity into the system.

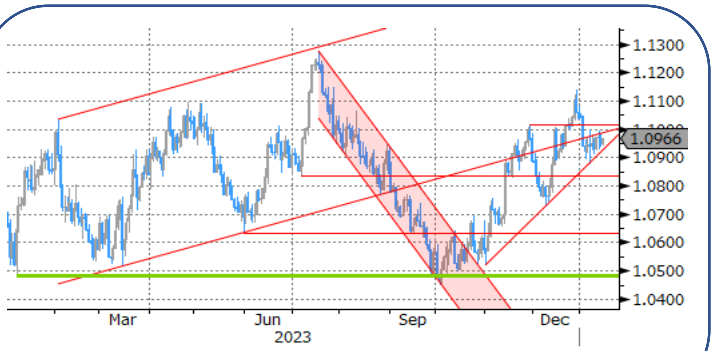
Graphs

GE 10y yield

Huge December bond rally on goldilocks scenario: avoiding a recession while the disinflationary process allows central bankers to pivot away from rate hikes to rate cuts. The **German 10-yr yield tested 2023 low at 1.92%.** ECB members push back against aggressive market pricing (150 bps cumulative rate cuts over 2024 and first 25 bps as early as April. Markets reluctantly pick up the message. **Structurally, we think the bond rally went too far.**

US 10y yield

The Fed's December gathering was a U-turn. Powell didn't fight market positioning with the updated FOMC dots pencilling in 75 bps of rate cuts this year. Market currently discount double that amount, starting the cutting the cycle in March. Market focus might switch from inflation to activity data. The December low at 3.78% is first (weak) support. **A sustained return above 4% is needed to change the technical picture.**



EUR/USD

The dollar lost out during the core bond rally as the Fed is more likely to start with policy rate cuts than the ECB, taking away interest rate support. Last year's high at 1.1276 is next important resistance for EUR/USD. A change of dynamics on bond markets is needed to improve the dollar's prospects.

EUR/GBP

Going nowhere. Extremely narrow trading range defined by 0.8493 and 0.8768 in place since May. Bank of England faces the most daunting challenge given more subdued eco outlook and higher inflation compared with the EU and the US. **Erring on the dovish (monetary policy) side could translate in a weaker UK currency,** bringing EUR/GBP back in the early 2023 range, roughly between 0.8750 and 0.90.

Calendar & Table

Monday, 15 January		Consensus	Previous
Canada			
16:30	BoC Business Outlook Future Sales (4Q)	--	14
16:30	BoC Overall Business Outlook Survey (4Q)	--	-3.5
Japan			
00:50	Money Stock M3 YoY (Dec)	1.70%A	1.70%
07:00	Machine Tool Orders YoY (Dec P)	--	-13.60%
UK			
01:01	Rightmove House Prices MoM/YoY (Jan)	1.30%A/0.70%A	-1.90%/-1.10%
EMU			
11:00	Industrial Production SA MoM/WDA YoY (Nov)	-0.30%/-6.00%	-0.70%/-6.60%
11:00	Trade Balance SA (Nov)	--	10.9b
Germany			
10:00	GDP NSA YoY (2023)	-0.30%	1.80%
10:00	Budget Maastricht % of GDP (2023)	-2.20%	-2.50%
Italy			
10:00	Trade Balance Total (Nov)	--	4699m
10:30	General Government Debt (Nov)	--	2867.7b
China			
02:20	1-Yr Medium-Term Lending Facility Rate	2.50%A	2.50%
02:20	1-Yr Medium-Term Lending Facilities Volume	995.0bA	1450.0b
Sweden			
08:00	**CPI MoM/YoY (Dec)**	**0.60%/4.30%**	**0.30%/5.80%**
08:00	CPIF MoM/YoY (Dec)	0.50%/2.20%	0.10%/3.60%
08:00	CPIF Excl. Energy MoM/YoY (Dec)	0.60%/5.20%	-0.50%/5.40%
Events			
15JAN	**US markets closed for Martin Luther King day**		
15:15	**ECB's Holzmann Speaks in Davos**		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	3,94	-0,03		US	4,14	-0,10	DOW	37592,98	-118,04
DE	2,18	-0,05		DE	2,52	-0,11	NASDAQ	14972,76	2,58
BE	2,72	-0,05		BE	2,56	-0,09	NIKKEI	35901,79	324,68
UK	3,79	-0,05		UK	4,16	-0,09	DAX	16704,56	157,53
JP	0,57	-0,04		JP	0,00	-0,01	DJ euro-50	4480,02	37,74

IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	2,66	3,71	3,84	Ester	3,9040	-0,0010			
5y	2,54	3,55	3,57	Euribor-1	3,8930	0,0130	SOFR-1	5,3321	-0,0003
10y	2,59	3,55	3,54	Euribor-3	3,9320	-0,0100	SOFR-3	5,3005	-0,0054
				Euribor-6	3,8960	-0,0240	SOFR-6	5,0855	-0,0380

Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1,0951	-0,0021		EUR/JPY	158,66	-0,75	CRB	264,38	0,28
USD/JPY	144,88	-0,41		EUR/GBP	0,8589	-0,0009	Gold	2051,60	32,40
GBP/USD	1,2753	-0,0007		EUR/CHF	0,9336	-0,0012	Brent	78,29	0,88
AUD/USD	0,6686	-0,0002		EUR/SEK	11,2552	-0,0010			
USD/CAD	1,341	0,0015		EUR/NOK	11,2681	-0,0460			

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